

February 3, 2004

The Honorable Bob Odell, Chairman  
Energy and Economic Development Committee  
Room 102, Legislative Office Building  
Concord, NH 03301

**Re: Senate Bill 488, establishing a study committee to study the effects of electric utility restructuring on state dams and the alternatives for the operation and maintenance of state-owned dams**

Dear Chairman Odell:

Thank you for the opportunity to comment on SB 488, which establishes a study committee to study the hydro-lease program of the State of New Hampshire, the effects that electric utility restructuring has had on the program and the State's Dam Maintenance Fund, and alternatives for operation and maintenance of state-owned dams. The Department of Environmental Services (DES) supports this bill, and looks forward to working with the study committee to develop recommendations for the continued operation and maintenance of state-owned dams and options for funding the State Dam Maintenance Fund.

The State of New Hampshire owns a total of 269 dams, which impound the most important recreational lakes in the state. Of these, 29 are High Hazard Dams, the failure of which would cause loss of life downstream, and 53 are Significant Hazard Dams, the failure of which would cause significant property damage downstream. Even the loss of any of the Low Hazard Dams that the state owns could cause significant economic losses to the state due to the loss of recreational opportunities and the devaluation of waterfront property associated with the dam.

Many of these dams were constructed in the mid-1800s to provide waterpower to fuel the industrialization of New Hampshire and Massachusetts, and most of the dams that the state owns are well over 100 years old. Because of their age, they require continued attention to maintain them in a safe condition. Given the number of dams the state owns and the normal design life of these structures, the state must perform major repairs or reconstruction on an average of five dams per year. The large number of dams the state owns also puts a large operations burden on the state. The outlets of each of these dams must be constantly managed so as not to cause flooding in the lakes and downstream, and to ensure that the recreation and other public benefits provided by the lakes are maintained.

The costs for the operation, maintenance, repair and reconstruction of these dams are funded from the State Dam Maintenance Fund. The sole source of revenue to the fund is rent payments that DES receives from leasing 12 of the dams that it owns to private hydropower developers to generate electricity at the sites. Under the terms of the leases, the rent that is paid to DES is a percentage of the revenue from the sale of power at the facilities. The percentage varies from lease to lease and ranges from 3.5 percent up to 38.5 percent. Public Service of New Hampshire (PSNH) is the purchaser of the power generated at 11 of the 12 sites. PSNH has long-term power purchase agreements with these facilities, under which they purchase the power at rates ranging from approximately 8¢ to approximately 17¢ per kilowatt-hour (kwh), which are above the current market rates of 3¢ to 4¢ per kwh. These power purchase agreements were generally established in the mid-1980s, and were approved by the Public Utilities Commission to encourage the development of alternative energy sources. Also, at the time that the agreements were established, the cost of power was projected to rise in the future to be at or above the power purchase rates.

A year ago, the Dam Maintenance Fund was projected to be solvent through 2015 based on projected revenues from these hydropower leases and projected expenditures on bond obligations and dam reconstruction projects. However, in 2002, PSNH initiated actions to renegotiate their power purchase agreements pursuant to RSA 374-F. This is the Electric Utility Restructuring legislation that directs utilities to take all reasonable measures to mitigate stranded costs, including the renegotiation of power purchase contracts. As part of that initiative, PSNH offered to buyout or buydown the power purchase agreements of the hydropower operators in the state from whom it purchases power. Seven of the lessees of the state-owned dams accepted the buyout or buydown offers.

Under the terms of the buyout offers, PSNH will continue to purchase power from the facilities, but will purchase it at market rates. In the case of the buydown offer, the power will be purchased at a reduced rate, slightly above the current market rate. In exchange, PSNH is making a lump sum payment to each of the operators. The lump sum payments are equal to 80% of the present value, computed using an interest rate of 10%, of the difference between what the operators would have received under the power purchase agreement and what they would receive under market rates, assuming past levels of power generation at the facilities for the remaining term of the power purchase agreements. For the buydown agreement, the lump sum payment was computed based on the difference between the rate in the power purchase agreement and the renegotiated reduced rate.

The lump sum payments made by PSNH to these seven lessees total nearly \$9.7 million. DES has maintained that a percentage of the lump sum payment is due to the state under the terms of the lease. That percentage amounts to over \$2.4 million. However, the lessees have maintained that the lump sum payment is not income received from the sale of electrical power produced at the facility, and is therefore not subject to the terms of the lease. The lessees have agreed to put the disputed amount in escrow, and the Attorney General's Office is currently

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litigating the matter on behalf of DES. In June 2003, the Merrimack County Superior Court ruled in favor of the lessees, and the case is currently under appeal in the New Hampshire Supreme Court.

If the State of New Hampshire loses the appeal, the Dam Maintenance Fund will be insolvent at the end of Fiscal year 2004. Even if the state wins and the \$2.4 million is paid to DES, the Dam Maintenance Fund will be insolvent at the end of Fiscal year 2007 because the payment is on only 80% of present value of the anticipated future revenue discounted using a relatively high interest rate.

Given this sudden, unexpected reduction in the funding source of the Dam Maintenance Fund, it is important to identify alternative sources of funding, as proposed in this bill, to ensure that the state's dams continue to be operated and maintained so that they do not pose a threat to life and property downstream and continue to provide economic and recreation benefits to the state. DES looks forward to working with the study committee on this effort.

Thank you for this opportunity to comment on this bill. Please call either me at 271-3503 or Jim Gallagher at 271-1961 if you have any questions or need additional information.

Very truly yours,

Michael P. Nolin  
Commissioner

cc: Senator Carl R. Johnson  
Senator John T. Gallus  
Senator Clifton C. Below  
Representative H. Charles Royce  
Representative Judith T. Spang  
Representative MaryAnn N. Blanchard